

ANALYSIS OF AMENDED BILL

Author: Leach Analyst: Paul Brainin Bill Number: AB 8
Related Bills: _____ Telephone: 845-3380 Amended Date: 04-28-98
Attorney: Doug Bramhall Sponsor: _____

SUBJECT: Minimum Tax/Dissolved Limited Liability Company's & Limited Liability Partnership's Percentage of Tax Based on Date of Dissolution

DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as introduced/amended _____.

☒ AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.

AMENDMENTS DID NOT RESOLVE THE DEPARTMENT'S CONCERNS stated in the previous analysis of bill as introduced/amended _____.

FURTHER AMENDMENTS NECESSARY.

☒ DEPARTMENT POSITION CHANGED TO Pending.

REMAINDER OF PREVIOUS ANALYSIS OF BILL AS INTRODUCED/AMENDED _____ STILL APPLIES.

☒ OTHER - See comments below.

SUMMARY OF BILL

This bill would amend sections of the Bank and Corporation Tax Law (B&CTL) of the Revenue and Taxation Code (R&TC) to prorate the final annually imposed tax on the dissolution or withdrawal of limited liability companies (LLCs) and limited liability partnerships (LLPs). The final tax amount shall be determined by multiplying the annual tax by the ratio that the months of the taxable year, preceding the effective date of dissolution or withdrawal, bear to the months of the taxable year.

SUMMARY OF AMENDMENT

The amendments, as proposed, replaced the language regarding the Legislative intent to examine the feasibility of changing the amount of the minimum franchise tax imposed under the B&CTL with the provisions discussed in this analysis.

EFFECTIVE DATE

This bill, as a tax levy, would be effective immediately and apply to taxable and income years beginning on or after January 1, 1998.

DEPARTMENTS THAT MAY BE AFFECTED:

____ STATE MANDATE

____ GOVERNOR'S APPOINTMENT

Board Position:

☐ S ☐ O
☐ SA ☐ OUA
☐ N ☐ NP
☐ NA ☐ NAR
☒ X PENDING

Agency Secretary Position:

☐ S ☐ O
☐ SA ☐ OUA
☐ N ☐ NP
☐ NA ☐ NAR
DEFER TO _____

GOVERNOR'S OFFICE USE

Position Approved _____
Position Disapproved _____
Position Noted _____

Department/Legislative Director Date
G. Alan Hunter **5/14/98**

Agency Secretary Date

By: _____ Date: _____

SPECIFIC FINDINGS

Under existing state law, every corporation that is organized or qualified to do business or is doing business in this state (whether organized in-state or out-of-state) is subject to the minimum franchise tax. Taxpayers must pay the minimum franchise tax only if it is more than their measured bank or corporation tax. For income years beginning on or after January 1, 1997, only taxpayers whose net income is less than approximately \$9,038 pay the minimum franchise tax because their measured tax would be less than \$800 ($\$9,038 \times 8.84\% = \799).

Under existing state law, every limited partnership (LP), LLC, and LLP that is organized or qualified to do business in this state (whether organized in this state or out-of-state) is subject to an annual tax of \$800. This amount is determined by reference to the amount provided in the minimum franchise tax statute. This annual tax is due until:

- (1) a certificate of cancellation is filed on behalf of an LP with the office of the Secretary of State (SOS);
- (2) a certificate of cancellation of registration or of articles of organization is filed on behalf of the LLC with the office of the SOS; or
- (3) an LLP files a notice of cessation with the SOS, withdraws its registration, or is dissolved and wound up (depending upon the type of LLP).

Existing state law declares the effective date of dissolution, withdrawal, or cancellation of a LLC is the date on which the certified copy of the court decree, judgment, or order declaring the LLC duly wound up and dissolved is filed in the office of the SOS or the date on which the certificate of winding up and dissolution is filed in the office of the SOS.

Existing state law does not allow the dissolution, withdrawal, or cancellation of any LLC or LLP to be effective unless the entity obtains from the Franchise Tax Board and files with the court, county clerk, or SOS, as the case may be, a tax clearance certificate indicating all taxes imposed are paid or secured.

This bill would allow LLCs and LLPs to pay a prorated tax in the year the LLC or LLP dissolves or withdraws. The prorated amount would be computed by dividing the months of the taxable year preceding the effective date of dissolution or withdrawal by the months of the taxable year.

Under current state law, LLCs also owe an annual fee based on the total income from all sources reportable to California in the taxable year. **This bill** would not affect the computation of the annual fee of a dissolving LLC. The fee is due and payable on the date the return of the LLC is required to be filed.

Policy Considerations

This bill would not provide equal treatment to LPs, corporations, and other entities that pay an annual tax such as real estate mortgage investment conduits (REMICs), financial assets securitization investment trusts (FASITs), qualified subchapter S subsidiaries (QSSSs), etc. The author's office has stated its intent to apply the same minimum tax proration provisions to corporations and LPs.

Implementation Considerations

Refunds would need to be made to LLCs that paid the applicable tax when due, but are dissolved or withdraw before the end of a 12-month taxable year. Issuing these refunds would create a minor additional workload for the department.

Technical Considerations

This bill amends B&CTL sections 23096, 23098, and 23099. These sections are no longer applicable. Personal Income Tax Law (PITL) sections 17946, 17948.1, and 17948.2 are the corresponding sections that are now applicable for LLCs and LLPs. The applicable laws for LPs also are in the PITL. The author's office has been made aware of this problem.

FISCAL IMPACT

Departmental Costs

This bill would not significantly impact the department's costs.

Tax Revenue Estimate

Based on data and assumptions discussed below, this bill would result in the revenue losses shown in the table.

Estimated Revenue Impact of AB 8 As Amended 4/28/98 [\$ In Millions]		
1998-99	1999-00	2000-01
(\$1)	(\$1)	(\$1)

The bill would be effective with income years beginning after December 31, 1997, with enactment assumed after June 30, 1998.

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this measure.

Tax Revenue Discussion

The revenue impact of this bill would be determined by the number of specified entities that dissolve or withdraw in any given year and owe a lesser amount of minimum tax than the prepaid \$800 currently required.

Applying a growth rate to each entity group projected the numbers of LLPs and LLCs filing in each year. A rate comparable to which corporations terminate annually (6%) was applied to determine the rate at which these entity types would potentially terminate. By assuming an average mid-year termination date, the above estimates were derived.

BOARD POSITION

Pending.

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FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO AB 8
As Amended April 28, 1998

AMENDMENT 1